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Supreme Court, U.S.
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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

MARIAN W. SHORT,
Petitioner,

vs.

BELLEVILLE SHOE MANUFACTURING COMPANY, *et al.*,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

For decades, the lower federal courts have applied the most analogous state law statute of limitations to suits under §10(b) of the Securities Exchange Act of 1934, and have also held that federal law, including the federal doctrine of equitable tolling, determines when the limitations period begins to run. The Seventh Circuit abandoned this practice, and applied instead the one-year limitations period of §12(2) of the 1933 Act, which also contains a three-year statute of repose. The Seventh Circuit's opinion follows a 1988 decision by the Third Circuit which has since been rejected by three other courts of appeals.

The questions presented are:

1. What is the appropriate statute of limitations and the appropriate tolling period in a federal civil action under §10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and Rule 10b-5 promulgated thereunder, 17 C.F.R. §240-10b-5?

2. In a federal civil action under §10(b) of the Securities Exchange Act of 1934, should federal courts continue to apply the closest analogous state law in selecting an appropriate statute of limitations or should they, for the sake of uniformity, apply a less analogous federal law?

3. In a federal civil action under §10(b) of the Securities Exchange Act of 1934, should federal courts continue to apply the deeply-rooted federal doctrines of equitable tolling and equitable estoppel, which are premised on the proposition that it is against equity and good conscience to allow anyone to take advantage of his own wrong, or should they instead adopt the three-year statute of repose contained in §12(2) of the 1933 Act?

LIST OF PARTIES

Petitioner before this Court is Marian W. Short. Respondents are Belleville Shoe Manufacturing Company, a corporation, and individuals Homer W. Weidmann, Eric R. Weidmann, Jane G. Weidmann and Kathryn W. McCoy. Respondent Belleville Shoe Manufacturing Company has no parent companies or non-wholly-owned subsidiaries known to Petitioner.

TABLE OF CONTENTS

	Page
Questions Presented	i
List of Parties	ii
Table of Authorities Cited	v
Opinions Below	1
Jurisdiction	2
The Statutory Provisions and Regulations Involved	2
Statement of the Case	4
Reasons for Granting the Writ	8
I. There Is a Clear Split in the Circuits	8
II. The Court Below Has Decided an Important Question of Federal Law Incorrectly and in Conflict With Decisions of This Court	11
A. Decisions of This Court Require Application of State Statutes of Limitation Unless Federal Law Clearly Provides a Closer Analogy	12
B. Claims Under §10(b) Do Not Fall Within the *DelCostello* Exception for Utilizing Federal Statutes Because §12(2) Does Not Clearly Provide a Closer Analogy and Because the Federal Policies at Stake and Practicalities of Litigation Do Not Make Selection of §12(2)'s Limitations Provisions Significantly More Appropriate for §10(b) Cases Than the State Blue Sky Law	16

C. Congressional Acquiescence in the Lower Federal Courts' Application of the Most Analogous State Limitations Provision to §10(b) Cases, and Principles of *Stare Decisis*, Require Reversal of the Seventh Circuit 21

D. The Decision Below Conflicts With Applicable Decisions of This Court Which Apply the Well-Accepted Doctrines of Equitable Tolling and Equitable Estoppel 23

Conclusion 26

Appendix

A. Opinion of the Court of Appeals A-1

B. Opinion of the District Court A-20

TABLE OF AUTHORITIES CITED

Page(s)

Cases:

Agency Holding Corp. v. Malley-Duff & Associates, 483 U.S. 143 (1987) ..... *passim*

Auto Workers v. Hoosier Cardinal Corp., 383 U.S. 696 (1966) 13,22,23

Bailey v. Glover, 88 U.S. (21 Wall.) 342 (1875) 24

Basic Inc. v. Levinson, 485 U.S. 224 (1988) 22

Bath v. Bushkin, Gaims, Gaines and Jonas, No. 88-2659, ____ F.2d ____, 1990 WL 128250 (10th Cir. Aug. 30, 1990) (per curiam) 10

Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) 11,18,19

Campbell v. City of Haverhill, 155 U.S. 610 (1895) 13

Cange v. Stotler & Co., 826 F.2d 581 (7th Cir. 1987) 26

In re Data Access Systems Securities Litigation, 843 F.2d 1537 (3rd Cir.) (in banc), *cert. denied sub nom. Vitiello v. Kahlowsky & Co.*, 488 U.S. 849 (1988) 6,8-11,19,21

DelCostello v. Teamsters, 462 U.S. 151 (1983) 12-20,24

Ebrahimi v. E.F. Hutton & Co., 852 F.2d 516 (10th Cir. 1988) 11

Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) 8,18,20,21

Exploration Co. v. United States, 247 U.S. 435 (1918) .. 24

Glus v. Brooklyn Eastern District Terminal, 359 U.S. 231 (1959) 25

Gurley v. Documation, Inc., 674 F.2d 253 (4th Cir. 1982) 10

Harris v. Union Electric Co., 787 F.2d 355 (8th Cir.), *cert. denied,* 479 U.S. 823 (1986) 10,11

Herman & MacLean v. Huddleston, 459 U.S. 375 (1983) ..8,18, 21,22

Holmberg v. Armbrecht, 327 U.S. 392 (1946).....13,23-24

IIT, an International Investment Trust v. Cornfeld, 619 F.2d 909 (2nd Cir. 1980) 10,11

Jensen v. Snellings, 841 F.2d 600 (5th Cir. 1988) 10,11

Maggio v. Gerard Freezer & Ice Co., 824 F.2d 123 (1st Cir. 1987) 10,11

McCluny v. Silliman, 28 U.S. (3 Pet.) 270 (1830)..... 12-13

Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran, 456 U.S. 353 (1982) 22

Nesbit v. McNeil, 896 F.2d 380 (9th Cir. 1990) 9-10

Norris v. Wirtz, 818 F.2d 1329 (7th Cir.), *cert. denied,* 484 U.S. 943 (1987) 17

O'Hara v. Kovens, 625 F.2d 15 (4th Cir. 1980), *cert. denied,* 449 U.S. 1124 (1981) 11

Osterneck v. E.T. Barwick Industries, Inc., 825 F.2d 1521 (11th Cir. 1987), *aff'd sub nom. Osterneck v. Ernst & Whinney,* 486 U.S. 1042 (1989) 11

Pinter v. Dahl, 486 U.S. 622 (1988) 17

Reed v. United Transportation Union, 109 S.Ct. 621 (1989) 15

Reeves v. Teuscher, 881 F.2d 1495 (9th Cir. 1989)..... 11

Roney & Co. v. Goren, 875 F.2d 1218 (6th Cir. 1989) ... 10

Schroeder v. Young, 161 U.S. 334 (1896) 25

Silverberg v. Thomson McKinnon Securites, Inc., 787 F.2d 1079 (6th Cir. 1986) 10,11

Singer v. Olympia Brewing Co., 878 F.2d 596 (2nd Cir. 1989), *cert. denied,* 110 S.Ct. 729 (1990) 10

Smith v. Duff and Phelps, Inc., 891 F.2d 1567 (11th Cir. 1990) 9

State of Ohio v. Peterson, Lowry, Rall, Barber & Ross, 651 F.2d 687 (10th Cir.), *cert. denied,* 454 U.S. 895 (1981) 11

United Mine Workers v. Gibbs, 383 U.S. 715 (1966) 6

Wachovia Bank & Trust Co. v. National Student Marketing Corp., 650 F.2d 342 (D.C. Cir. 1980), *cert. denied,* 452 U.S. 954 (1981) 10,11

Wilson v. Garcia, 471 U.S. 261 (1985) 9

Statutes and Rules:

Clayton Act, 15 U.S.C. §15(a) 14,19

Clayton Act, 15 U.S.C. §15b 9,14,24-25

Insider Trading and Securities Fraud Enforcement Act of 1988, §20A(b)(4), 15 U.S.C. §78t-1(a) 19

Labor Management Relations Act, §301, 29 U.S.C. §185 13

Labor Management Reporting and Disclosure Act, 29 U.S.C. §411(a)(2) 15

National Labor Relations Act, §10(b), 29 U.S.C. §160(b) 13

Racketeer Influenced and Corrupt Organizations Act (RICO), 15 U.S.C. §1964(c) 6,9,14,15,19

Securities Act of 1933, 15 U.S.C. §77a *et seq.*

Section 12(2), 15 U.S.C. §77*l*(2) ..... *passim*

Section 13, 15 U.S.C. §77m 6,9,18,23

Securities Exchange Act of 1934, §10(b), 15 U.S.C. §78j(b) ..... *passim*

Rule 10b-5, 17 C.F.R. §240.10b-5 ..... *passim*

Illinois Blue Sky Law, Ill. Rev. Stat. Ch. 121½, ¶137.12 ...3,4, 16,17

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Petitioner Marian W. Short respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit entered July 30, 1990.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit is reported at 908 F.2d 1385, and is reprinted in the Appendix (App. A-1). The memorandum decision of the United States District Court for the Southern District of Illinois (Beatty, J.), granting Respondents' motion to dismiss Petitioner's amended complaint, is unreported and is reprinted in the Appendix (App. A-20).

JURISDICTION

The United States Court of Appeals for the Seventh Circuit entered its judgment on July 30, 1990. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS AND REGULATIONS INVOLVED

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b):

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —
>
> * * *
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

SEC Rule 10b-5, 17 C.F.R. §240.10b-5:

> Employment of manipulative and deceptive devices.
>
> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> > (a) To employ any device, scheme, or artifice to defraud,
> >
> > (b) To make any untrue statement of a material fact or omit to state a material fact necessary in order to

make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

Portions of Illinois Blue Sky Law, Ill.Rev.Stat. Ch. 121½, ¶¶137.12 and 137.13:

137.12. Violation

§12. Violation. It shall be a violation of the provisions of this Act for any person:

* * *

F. To engage in any transaction, practice or course of business in connection with the sale or purchase of securities which works or tends to work a fraud or deceit upon the purchase or seller thereof;

* * *

I. To employ any device, scheme or artifice to defraud in connection with the sale or purchase of any security, directly or indirectly;

* * *

137.13. Civil remedies

* * *

D. No action shall be brought for relief under this Section or upon or because of any of the matters for which relief is granted by this Section after 3 years from the date of sale; provided, that if the party bringing the action neither knew nor in the exercise of reasonable diligence

should have known of any alleged violation of subsection E, F, G, H, I or J or Section 12 of this Act which is the basis for the action, the 3 year period provided herein shall begin to run upon the earlier of:

(1) The date upon which the party bringing such action has actual knowledge of the alleged violation of this Act; or

(2) the date upon which the party bringing such action has notice of facts which in the exercise of reasonable diligence would lead to actual knowledge of the alleged violation of this Act; but in no event shall the period of limitation so extended be more than 2 years beyond the expiration of the 3 year period otherwise applicable.

* * *

STATEMENT OF THE CASE

Petitioner brought this action in February 1989 against Respondent Belleville Shoe Manufacturing Company ("Belleville Shoe"), a closely-held corporation, and its officers and directors, alleging that they had defrauded her in a redemption of her 550 shares of stock in May, 1977. Petitioner alleged, *inter alia,* that the redemption of her shares was part of a scheme to defraud in violation of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b) (hereinafter "§10(b)"), and Rule 10b-5 promulgated thereunder, 17 C.F.R. §240.10b-5.

Petitioner alleged that the fraud included false representations by Respondent Homer W. Weidmann, Petitioner's brother and a director of Belleville Shoe. At the time of the misrepresentations, and until late 1988, Homer Weidmann was Petitioner's confidant and business advisor. Pursuant to a power of attorney, Homer acted in Petitioner's behalf in all business dealings. The false representations by Homer included

statements that Belleville Shoe was in financial difficulty, that the prospects of recovery were not good, and that if Petitioner redeemed her stock, she would have the opportunity to repurchase the shares. Homer Weidmann concealed from Petitioner the fact that the redemption price was significantly less than the fair value of the stock and that the redemption price was not based on any accepted formula for valuation of shares, but was determined by the amount of money needed by Petitioner to satisfy an obligation to the First National Bank of Belleville. In fact, Belleville Shoe was not in financial difficulty. Current financial information showed that the company would show a profit for the year 1977 and that its profitability would improve in the foreseeable future. These and other intentional misrepresentations, concealments and deceptions in connection with the redemption transaction are alleged to have been made by Homer Weidmann individually and on behalf of Belleville Shoe and its other officers and directors, Respondents Eric R. Weidmann, Jane G. Weidmann and Kathryn W. McCoy. Petitioner Marian Short relied on defendants' statements and redeemed her shares.

Petitioner alleged that she did not know of these wrongful acts at the time of the redemption transaction and, indeed, could not have learned of them by the exercise of due diligence until the company's records were examined by her attorney on October 4, 1988. Petitioner alleged that she could not have learned of these violations earlier because of a number of factors, including her continued confidence and trust in Respondents (especially Homer Weidmann), who were in a fiduciary position to her, and because of positive steps and active conduct by Respondents to conceal their wrongful actions, including statements to Petitioner after redemption that she had obtained a fair and equitable price (Amended Complaint, ¶ 5).

Respondents moved to dismiss on the ground that, *inter alia,* the securities law claims were barred by limitations. The district court entered its Order dismissing the action on September 25,

1989. The court held that Petitioner had pleaded facts entitling her to the benefit of federal equitable tolling. App. A-25. The court held that, nevertheless, the securities act claims were time-barred as of two years after the amendment of the applicable Illinois statute of limitations in 1986. App. A-24.[1]

On appeal to the Seventh Circuit Respondents argued, for the first time, that the court should abandon its time-honored approach of applying the state blue sky law statute of limitations period, supplemented by the federal doctrine of equitable tolling, to §10(b) claims. Instead, Respondents argued that the court should adopt the new approach of the Third Circuit announced in *In re Data Access Systems Securities Litigation,* 843 F.2d 1537 (3rd Cir.) (in banc), *cert. denied sub nom. Vitiello v. Kahlowsky & Co.,* 488 U.S. 849 (1988). The Seventh Circuit below agreed and held that Petitioner's claims would be governed not by state limitations law and federal tolling principles, but rather by §13 of the 1933 Securities Act, 15 U.S.C. §77m, which is the statute of limitations for actions by purchasers of securities under §12(2) of the 1933 Act, 15 U.S.C. §77*l*(2). That limitations period is one year after discovery of the violation, and it contains a built-in three-year statute of repose, which, the court of appeals held, barred Petitioner's claims. The Seventh Circuit acknowledged that its decision overturned existing law in that circuit, App. A-8, and contributed to an "established conflict among the circuits," App. A-7.

Judge Posner joined the Seventh Circuit's opinion, but also authored a separate concurrence expressing dissatisfaction with all forms of statute of limitations borrowing. Judge Posner sug-

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[1] Counts I and V were the two counts brought under §10(b). The district court also dismissed Counts II, III and IV, which were brought under RICO, but these counts are not the subject of this Petition. The district court did not address the merits of the four remaining counts, which were pendent claims under state law, but rather dismissed them under *United Mine Workers v. Gibbs,* 383 U.S. 715 (1966).

gested that Congress should adopt a rule requiring every statute to contain a statute of limitations, and create an agency empowered to adopt regulations engrafting statutes of limitations onto statutes that lack them. App. A-15.

REASONS FOR GRANTING THE WRIT

For decades, the various courts of appeals have held that because §10(b) contains no statute of limitations, the limitations period of the forum state applies to §10(b) actions. This Court has twice specifically acknowledged this practice. *See Herman & MacLean v. Huddleston,* 459 U.S. 375, 384 n.18 (1983); *Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 210 n.29 (1976). Equally entrenched in our jurisprudence is the practice of applying the federal doctrine of equitable tolling to actions under federal law which, like §10(b), borrow state limitations periods. Under federal equitable tolling, federal law determines the *time* when the applicable state limitations period begins to run.

In 1988, the Third Circuit bolted from this settled practice and held that the statute of limitations in §10(b) actions would henceforth be the one-year statute and three-year statute of repose found in §13 of the Securities Act of 1933. *In re Data Access Systems Litigation,* 843 F.2d 1537 (3rd Cir.) (in banc), *cert. denied sub nom. Vitiello v. Kahlowsky & Co.,* 488 U.S. 849 (1988). The Third Circuit's *Data Access* decision has since been explicitly rejected by the Eleventh, Ninth and Tenth Circuits. The Seventh Circuit, in the case at bar, embraces *Data Access* in an opinion which conflicts with the recent decisions of this Court upon which it purports to rely. This case is an appropriate vehicle for the Court to eliminate the confusion regarding the statute of limitations and the period of repose in litigation involving §10(b), an important and widely-used statute for vindicating wrongdoing in the purchase and sale of securities.

I.

There Is a Clear Split in the Circuits

The Seventh Circuit has joined the Third in rejecting a long line of cases in every other circuit (and, indeed, overturning clear precedents in their own circuits) holding that the most appropriate statute of the forum state supplies the limitations

period under §10(b), and that the limitations period is subject to federal estoppel and tolling principles which determine when the limitations period begins to run. The Seventh Circuit below and *Data Access* have announced, as new law, that §13 of the 1933 Act, as amended, 15 U.S.C. §77m, the statute governing cases under §12(2) of the 1933 Act, 15 U.S.C. §77*l*(2), will now apply to §10(b) actions, and therefore the limitations period is a one-year statute with a three-year statute of repose.

Data Access was decided in April, 1988. Since that time the Eleventh, Ninth and Tenth Circuits have addressed the issue of limitations in §10(b) actions and expressly rejected the holding of *Data Access*. In *Smith v. Duff and Phelps, Inc.*, 891 F.2d 1567 (11th Cir. 1990), the panel was urged to follow *Data Access*, but it declined to overrule previous panels. Appellant in that case argued that this Court's recent decision in *Agency Holding Corp. v. Malley-Duff & Associates*, 483 U.S. 143 (1987), which applied the four-year Clayton Act statute of limitations to RICO cases, required re-examination of existing precedent.[2] The Eleventh Circuit panel rejected this argument and held that neither *Agency Holding* nor *Wilson v. Garcia*, 471 U.S. 261 (1985), required the court to overrule its prior holdings. On May 10, 1990, the Eleventh Circuit denied rehearing en banc, 904 F.2d 712 (11th Cir. 1990).

Similarly, the Ninth Circuit squarely rejected *Data Access* in *Nesbit v. McNeil*, 896 F.2d 380 (9th Cir. 1990), holding that it was bound by clear precedent applying state statutes of limitation to §10(b) cases, and was not permitted to follow *Data Access*. The Ninth Circuit then observed that in any event, the recent *Agency Holding* and *Wilson* decisions of this Court "do

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[2] This is the same argument advanced by the Seventh Circuit in its opinion below.

not compel a reassessment and reversal of our position." 896 F.2d at 384.[3]

In *Bath v. Bushkin, Gaims, Gaines & Jonas*, No. 88-2659, ____ F.2d ____, 1990 WL 128250 (10th Cir. Aug. 30, 1990) (per curiam), the Tenth Circuit joined the Eleventh and Ninth in rejecting *Data Access*. The district court in *Bath* had relied on *Data Access* in dismissing a §10(b) claim as time-barred; the court of appeals reversed and held, "While we recognize the simplicity of having a single limitations period for all §10(b) and Rule 10b-5 claims, the rule in this circuit is that such suits are subject to the appropriate limitations statute of the state in which the alleged violation occurred." Slip op. at 2.

In addition to the Eleventh, Ninth and Tenth Circuit cases described above, the decision below and *Data Access* also conflict with decisions in every other circuit, which recognize that state law, not other federal securities statutes, governs limitations under §10(b). *E.g., Maggio v. Gerard Freezer & Ice Co.*, 824 F.2d 123 (1st Cir. 1987); *IIT, an International Investment Trust v. Cornfeld*, 619 F.2d 909 (2nd Cir. 1980); *Gurley v. Documation, Inc.*, 674 F.2d 253 (4th Cir. 1982); *Jensen v. Snellings*, 841 F.2d 600 (5th Cir. 1988); *Silverberg v. Thomson McKinnon Securities, Inc.*, 787 F.2d 1079 (6th Cir. 1986); *Harris v. Union Electric Co.*, 787 F.2d 355 (8th Cir.), *cert. denied*, 479 U.S. 823 (1986); *Wachovia Bank & Trust Co. v. National Student Marketing Corp.*, 650 F.2d 342 (D.C. Cir. 1980), *cert. denied*, 452 U.S. 954 (1981).

Moreover, the decision below, by adopting a federal statute of limitations which contains a built-in statute of repose, jettisons

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[3] In addition, the Sixth and Second Circuits have recently observed in dictum the general rule that state law supplies the limitations period for cases under §10(b), and acknowledged *Data Access's* contrary position. *See Roney & Co. v. Goren*, 875 F.2d 1218, 1223 (6th Cir. 1989); *Singer v. Olympia Brewing Co.*, 878 F.2d 596, 599 (2nd Cir. 1989), *cert. denied*, 110 S.Ct. 729 (1990).

the well-established rule that the federal doctrine of equitable tolling applies to implied rights of action under §10(b).[4] Nearly every other circuit has recently acknowledged the existence of this rule, which prevents a wrongdoer from profiting by his own fraud. *E.g., Maggio, IIT, Jensen, Silverberg, Harris,* and *Wachovia Bank & Trust, supra; Reeves v. Teuscher,* 881 F.2d 1495 (9th Cir. 1989); *Osterneck v. E.T. Barwick Industries, Inc.,* 825 F.2d 1521 (11th Cir. 1987), *aff'd sub nom. Osterneck v. Ernst & Whinney,* 486 U.S. 1042 (1989); *State of Ohio v. Peterson, Lowry, Rall, Barber & Ross,* 651 F.2d 687 (10th Cir.), *cert. denied,* 454 U.S. 895 (1981); *Ebrahimi v. E.F. Hutton & Co.,* 852 F.2d 516 (10th Cir. 1988) (relying on §10(b) cases in applying doctrine to Commodity Exchange Act); *cf. O'Hara v. Kovens,* 625 F.2d 15 (4th Cir. 1980), *cert. denied,* 449 U.S. 1124 (1981) (looking to state law tolling principles). The Seventh Circuit below and *Data Access* have deserted these established principles and, ironically, have created a conflict among the circuits in the name of "uniformity."

II.

The Court Below Has Decided an Important Question of Federal Law Incorrectly and in Conflict With Decisions of This Court

It can hardly be gainsaid that the questions presented herein — the statute of limitations and period of repose in a §10(b) and Rule 10b-5 case — are important questions of federal law. The Court has described Rule 10b-5 as a "judicial oak which has grown from little more than a legislative acorn." *Blue Chip Stamps v. Manor Drug Stores,* 421 U.S. 723, 737 (1975).

The decision below conflicts with a long line of cases holding that state statutes provide the limitations period for federal

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[4] The district court held that plaintiff had adequately pleaded facts which give rise to the federal equitable tolling doctrine, *i.e.,* defendants' active concealment of their fraud (App. A-25).

rights of action that do not contain a statute of limitations. It conflicts even with the cases upon which it purports to rely, notably *Agency Holding Corp. v. Malley-Duff & Associates,* 483 U.S. 143 (1987), and *DelCostello v. Teamsters,* 462 U.S. 151 (1983), which articulate narrow exceptions to the rule. The Seventh Circuit's opinion misinterprets the application of these exceptions as an "invitation" to forge fundamental changes in the relationship between our state and federal legal systems. The court of appeals' opinion ignores longstanding Congressional acquiescence in the holdings of lower federal courts that §10(b) claims are governed by the most analogous state statute of limitations, as supplemented by the federal doctrine of equitable tolling. Finally, the decision below conflicts with numerous other decisions of this Court applying the deeply rooted federal doctrines of equitable tolling and equitable estoppel, which hold that it is against equity and good conscience to allow a person to profit by his own wrongdoing.

A.

Decisions of this Court Require Application of State Statutes of Limitation Unless Federal Law Clearly Provides a Closer Analogy

Application of state statutes of limitation to federal causes of action not containing limitations provisions is a time-honored practice. The Court described it as "well settled" in *McCluny v. Silliman,* 28 U.S. (3 Pet.) 270 (1830):

> It is a well settled principle that a statute of limitations is the law of the forum, and operates upon all who submit themselves to its jurisdiction.
>
> In the thirty-fourth section of the judiciary act of 1789, it is provided, "that the laws of the several states, except where the Constitution, treaties or statutes of the United States shall otherwise require or provide, shall be regarded as rules of decision in trials at common law, in the Courts of the United States, in cases where they apply."

> Under this statute, the acts of limitation of the several states, where no special provision has been made by Congress, form a rule of decision in the Courts of the United States, and the same effect is given to them as is given in the state Courts.

Id. at 276-77. Following *McCluny*, the Court continued to apply this doctrine on a consistent basis. In *Campbell v. City of Haverhill*, 155 U.S. 610 (1895), the Court held that because Congress omitted a limitations provision in a revision of a patent law, limitations in an action for infringement was governed by state law. "Is it not more reasonable to presume that congress, in authorizing an action for infringement, intended to subject such action to the general laws of the state applicable to actions of a similar nature?" 155 U.S. at 616. In *Holmberg v. Armbrecht*, 327 U.S. 392, 395 (1946), the Court again observed the "implied absorption of State statutes of limitation within the interstices of the federal enactments," but also held that this absorption does not preclude a federal court from also applying the federal doctrine of equitable tolling. *See* part II, D, *infra*.

In *Auto Workers v. Hoosier Cardinal Corp.*, 383 U.S. 696 (1966), the Court held that a union's suit against an employer for breach of a collective bargaining agreement under §301 of the Labor Management Relations Act, 29 U.S.C. §185 ("§301"), which contains no statute of limitations, was properly governed by the Indiana six-year statute for actions on unwritten contracts. The Court rejected the argument that the action should be governed by the six-month limitations provision governing unfair labor practice proceedings, 29 U.S.C. §160(b).

The Court did apply the six-month unfair labor practice statute of limitations in *DelCostello v. Teamsters*, 462 U.S. 151 (1983), which, unlike *Hoosier*, was a "hybrid" action against the employer for breach of the collective bargaining agreement and against the union for breach of its duty of fair representation. Because each facet of this hybrid §301/fair representation

action would be governed by a different limitations period under state law, and because there was "no close analogy in ordinary State law," 462 U.S. at 165, the Court held that the parallel to the federal unfair labor practice statute was more apt than any state statute, and its six-month limitations period therefore governed. The Court emphasized:

> [T]here is not always an obvious state-law choice for application to a given Federal cause of action; *yet resort to state law remains the norm for borrowing of limitations periods.* Nevertheless, when a rule from elsewhere in federal law *clearly provides a closer analogy than available state statutes,* and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking, we have not hesitated to turn away from state law.

462 U.S. at 171-72 (emphasis added).

The Court applied the *DelCostello* exception to the general rule again in *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), a case heavily relied upon by the Seventh Circuit. In *Agency Holding* the Court held that the four-year statute of limitations under the Clayton Act, 15 U.S.C. §15b, applied to civil cases under RICO, 18 U.S.C. §1964(c). The Court held that the Clayton Act provided the "*closest* analogy to civil RICO," 483 U.S. at 150 (emphasis added), because of the statutes' similarity in purpose and structure. Both statutes provided civil remedies, including treble damages and attorneys' fees, to a person "injured in his business or property by reason of" a violation. *Compare* 15 U.S.C. §15(a) with 18 U.S.C. §1964(c). The similarities in these statutes, the Court observed, were not accidental; Congress used an "anti-trust model" to develop RICO, and the "bill's sponsor described the civil enforcement remedy as 'another example of the antitrust remedy being adapted for use against organized criminality, 116 Cong. Rec. 35295 (1970)' . . . ." 483

U.S. at 152. Moreover, the Court observed that "there is no comparable single state law analogue to RICO." *Id.*

The Seventh Circuit clearly erred in holding that *DelCostello* and *Agency Holding* "call for fresh examination" of the limitations period in securities cases, App. A-4, and that "[a]lthough *stare decisis* has it claims, *Agency Holding* took a bold step that invites the inferior federal courts to reconsider their handling of adjacent fields," App. A-7. *Agency Holding* was not a "bold step;" it was simply an appropriate application of the rule announced in *DelCostello,* that where federal law "clearly provides a closer analogy" and where the "federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking," a federal rule should be applied. 462 U.S. at 172. Otherwise, "resort to state law remains the norm for borrowing of limitations periods." *Id.* at 171.

That *Agency Holding* was not an "invitation" for the lower federal courts to discard existing law is demonstrated by *Reed v. United Transportation Union,* 109 S.Ct. 621 (1989). In that case the Court held that claims by a union member under §101(a)(2) of the Labor Management Reporting and Disclosure Act, 29 U.S.C. §411(a)(2), alleging that the union violated its members' free speech rights, are governed by the *state's* general or residual personal injury statutes of limitation. The Court reasoned that such claims were "readily analogized" to state personal injury actions, and that resort to federal law was unnecessary. The *Reed* Court reiterated that *DelCostello* "recognized a closely circumscribed exception to the general rule that statutes of limitations are to be borrowed from state law." 109 S.Ct. at 625.

B.

Claims Under §10(b) Do Not Fall Within the *DelCostello* Exception for Utilizing Federal Statutes Because §12(2) Does Not Clearly Provide a Closer Analogy and Because the Federal Policies at Stake and Practicalities of Litigation Do Not Make Selection of §12(2)'s Limitations Provisions Significantly More Appropriate for §10(b) Cases Than the State Blue Sky Law

The first branch of the *DelCostello* test for resort to federal instead of state law requires that a "rule from elsewhere in federal law clearly provides a closer analogy than available state statutes." 462 U.S. at 172. The court below found a "closer" analogy to §10(b) in §12(2), in spite of the fact that: (1) the class of persons who can bring §10(b) suits is broader than the class of potential §12(2) plaintiffs; (2) the class of potential defendants in §10(b) suits is *far* broader than that of potential §12(2) defendants; and (3) there are significant procedural and proof distinctions between the two statutes.

By the statute's very terms, the prohibitions of §12(2), which provides a remedy for materially incorrect or misleading selling literature and oral communications in the sale of a security, apply only to the conduct of persons *selling* or offering to sell securities.[5] By contrast, the Illinois Blue Sky Law, like Rule 10b-5, prohibits fraudulent conduct by sellers *and* purchasers of securities:

> It shall be a violation of the provisions of this Act for any person:
>
> * * *

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[5] The Seventh Circuit noted, App. A-9, that Petitioner could not have sued under §12, because that section is addressed only to conduct by sellers of securities, whereas in the instant case, Defendants-Respondents were purchasers.

> F. To engage in any transaction, practice or course of business in connection with the *sale or purchase* of securities which works or tends to work a fraud or deceit *upon the purchaser or seller thereof*;
>
> * * *
>
> I. To employ any device, scheme or artifice to defraud in connection with the *sale or purchase* of any security, directly or indirectly;
>
> * * *

Ill.Rev.Stat. Ch. 121 1/2, ¶137.12 (emphasis added).[6]

While there is some overlap in §10(b) and §12(2), in that sellers who make false representations about securities might be liable under both statutes, the universe of potential §10(b) defendants is far greater than that of potential §12(2) defendants. Liability under §12 is limited to "Any person who . . . offers or sells a security. . . ." *See Pinter v. Dahl*, 486 U.S. 622 (1988). By contrast, §10(b) prohibits conduct "in connection with the purchase or sale of" securities. Liability under §10(b) can be predicated upon aiding and abetting, conspiracy, and the like, and §10(b) cases are frequently brought against accountants, attorneys, and others who neither "offer" nor "sell" securities. *See* 5A A. Jacobs, *Litigation and Practice Under Rule 10b-5*, §40 (rev. ed. 1990).

The Seventh Circuit, aligning itself with the Third, glossed over another fundamental difference between §10(b) and §12(2)

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[6] Although the Illinois Blue Sky Law does not provide a private civil *remedy* to sellers of securities, neither does §12(2). In any event, the Seventh Circuit, before it abandoned its rule in the case at bar, held that the Illinois Blue Sky Law limitations period applies to §10(b) claims by sellers. *See Norris v. Wirtz*, 818 F.2d 1329 (7th Cir.), *cert. denied*, 484 U.S. 943 (1987).

in coming to its erroneous conclusion that under *DelCostello*, §12(2) "clearly provides a closer analogy than available state statutes." 462 U.S. at 172. To prove a claim under §12(2), only negligence must be shown, while to prove a claim under §10(b), scienter must be shown. Petitioner submits that the different proof requirements under the two sections are a critical reason for the different statutes of limitation. Under §12(2), a statute of limitations with a statute of repose is entirely reasonable, since a defendant can be liable without any intentional wrongdoing. Thus, after some period the liability of the defendant should be extinguished. The §10(b) case is very different because to prove a claim the plaintiff must show intentional wrongdoing. To extinguish liability after a fixed period in §10(b) actions, without regard to whether the defendant has continued the deception successfully beyond the fixed period, is to reward the deceiver for continuing the deception.

The Court has noted this distinction in prior cases. In *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), the Court, in determining that scienter is required in actions under §10(b), stated that §12(2) claims are subject to "significant procedural restrictions not applicable under §10(b)." 425 U.S. at 209. These restrictions include the "substantially shortened" statute of limitations provided by §13 of the 1933 Act, as amended, 15 U.S.C. §77m, which governs claims under §12(2). The *Ernst & Ernst* Court observed that the §10(b) remedy "has no comparable restrictions," and stated that because §10(b) is silent, the limitations law of the forum applies. Significantly, the Court also noted that these state statutes "usually are longer than the period provided under §13 [the §12(2) limitations provision utilized by the Seventh Circuit]." 425 U.S. at 210 and n.29. Again, in *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983), the Court noted that the state limitations periods are "usually longer than the period provided for §11 actions." 459 U.S. at 384 n.18. *Cf. Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730 n.4 (1975) (referring to the "contrast between the provisions of Rule 10b-5 and the numerous carefully drawn ex-

press civil remedies provided in the acts of both 1933 and 1934," including §12).

The very structure of the Seventh Circuit's opinion betrays the flaw of its analysis. The court of appeals first determined, in part IA of its opinion, that the *DelCostello* exception applied and that some federal law "clearly provides a closer analogy," before it even examined (in part IB) what it perceived to be the two choices of federal statutes available — §12(2), and the five-year limitations provision contained in the Insider Trading and Securities Fraud Enforcement Act of 1988, which added §20A(b)(4) to the 1934 Act, 15 U.S.C. §78t-1(a). The court of appeals noted that the Securities and Exchange Commission prefers the §20A approach, App. A-5, but that *Data Access* had chosen the §12(2) limitations period. The Seventh Circuit was "reluctant to depart from the statute that will be employed in the third circuit," App. A-10.

The two factors which drove the Court's decision in *Agency Holding* — the clear patterning of RICO after the Clayton Act and the absence of any satisfactory state law analogue — are not present in the instant case. Section 10(b) clearly is not patterned after §12(2). And the state blue sky laws provide a more than satisfactory analogue. Accordingly, §12(2) does not "clearly provide[] a closer analogy," and the Seventh Circuit erred in its application of the narrow exception in *DelCostello* and *Agency Holding* to the case at bar. Such an application would swallow the rule long adhered to by this Court that *state* law fills the gap where Congress has not enacted a statute of limitations for a federal cause of action.

Neither does §10(b) satisfy the second *DelCostello* requirement for departing from the norm and borrowing federal law — "when the federal policies at stake and the practicalities of litigation make [the rule from elsewhere in federal law] a significantly more appropriate vehicle for interstitial lawmaking." 462 U.S. at 172. The opinion below does not identify *any* federal policy at

stake that makes the §12(2) rule "more appropriate." Petitioner submits that the pertinent federal policy at stake is that of compensating individuals who have been swindled in connection with the purchase or sale of securities, a policy which makes the Seventh Circuit's selection of the §12(2) limitations period singularly inappropriate. The federal courts should not reward a wrongdoer's concealment of his fraud through the use of a period of limitations and repose which does not take into account the time when the plaintiff discovers the fraud perpetrated by the defendant.

The opinion below focuses on the "practicalities of litigation," which, for the Seventh Circuit, all boil down to uniformity. The court of appeals bemoans the "uncertainty" and "lack of uniformity" (App. A-6) to which its decision has, ironically, added. But this argument proves too much. If uniformity is the paramount objective, then a federal limitations period will almost always be chosen when a federal statute lacks an express limitations provision. Under the Seventh Circuit's analysis, federal law will displace state limitations periods in all but the most isolated instances where the federal cause of action is so novel that nothing else in the federal code can be remotely analogized to it. The court of appeals' approach ignores the Court's reminders in *DelCostello* and *Agency Holding* that "resort to state law remains the norm for borrowing of limitations periods." 462 U.S. at 171, 483 U.S. at 148.

Petitioner submits that the "practicalities of litigation" require adherence to the traditional rule of borrowing state-law limitations periods in §10(b) cases, and continuing to apply the federal doctrine of equitable tolling. Allegations of scienter — that is, "intent to deceive, manipulate, or defraud" — are required for a §10(b) action. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976) (footnote omitted). By contrast, §12(2) of the 1933 Act, the statute chosen by the court below, contains no such requirement and allows recovery for simple negligence. *Id.* at 208. Petitioner submits that it is not "significantly more appropriate" to

borrow a federal limitations period from a statute that permits recovery based on negligence and then use it in cases under a different statute which requires proof of intent. A defendant who possesses the requisite scienter to violate §10(b) is, logically, more likely to conceal the fraud from his victim. Indeed, before *Data Access*, the lower federal courts uniformly held that such concealment tolled the running of the statute of limitations. The decision below, by borrowing the short limitations period of §12(2), which cuts off tolling, would deprive victims of their remedy and reward fraud. The "practicalities of litigation" — *i.e.*, the common-sense fact that §10(b) violations are frequently covered up by their perpetrators — suggest that the courts should eschew the §12(2) statute of repose in favor of the well-settled practice of applying state limitations law plus the federal equitable tolling doctrine.

C.

Congressional Acquiescence in the Lower Federal Courts' Application of the Most Analogous State Limitations Provision to §10(b) Cases, and Principles of Stare Decisis, Require Reversal of the Seventh Circuit

The Seventh Circuit acknowledged that the application of state-law limitations periods to federal causes of action is so routine for the federal courts that for many years they "did this on auto-pilot." App. A-3. Petitioner submits that principles of *stare decisis* require maintaining such a well-established rule, at least with respect to statutes for which it has been routinely applied, until Congress dictates otherwise.

The Seventh Circuit acknowledged that its decision departed from this Court's dictum in *Ernst & Ernst v. Hochfelder*, 425 U.S. at 210, n.29, and *Herman & MacLean v. Huddleston*, 459 U.S. at 384 n.18, and also from well-settled practice followed by every other circuit but the Third. The application of state law limitations principles to rule 10b-5 cases is a longstanding one, and Congress has not seen fit to change it. This alone provides a

compelling reason for the employment of *stare decisis* and reversal of the court below. The Seventh Circuit's observation that "Congress has not been silent" on this issue because the "securities acts are jammed with statutes of limitation," App. A-3, does not support its result. Instead, it shows that Congress knows how to enact such statutes, but has chosen not to for §10(b), and acquiesced in the decisions of the lower federal courts over a period of several decades. "[W]e can generally assume that Congress intends by its silence that we borrow state law." *Agency Holding*, 483 U.S. at 147. *Cf. Basic Inc. v. Levinson*, 485 U.S. 224, 230-31 (1988) (observing that "judicial interpretation and application, legislative acquiescence, and the passage of time have removed any doubt that a private cause of action exists for a violation of §10(b) and Rule 10b-5").

This is particularly true in light of the fact that in 1975, Congress "comprehensively revised the securities laws" and enacted the " 'most substantial and significant revisions of this country's Federal securities laws since the passage of the Securities Exchange Act in 1934.' " *Herman & MacLean*, 459 U.S. at 384-85 (citation omitted). Those revisions did not include any §10(b) statute of limitations.[7]

> [S]tate statutes have repeatedly supplied the periods of limitations for federal causes of action where federal legislation has been silent on the question . . . . *Yet when Congress has disagreed with such an interpretation of its*

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[7] The Court rejected an argument in *Herman & MacLean* that the existence of an express remedy under §11 eliminated an implied remedy under §10(b) for the same conduct since the courts had held for years that the statutes were cumulative, not mutually exclusive. "In light of this well-established judicial interpretation, Congress' decision to leave §10(b) intact suggests that Congress ratified the cumulative nature of the §10(b) action. *See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 381-82 (1982)." *Herman & MacLean*, 459 U.S. at 385-86.

> *silence*, it has spoken to overturn it by enacting a uniform period of limitations . . . . Against this background, we cannot take the omission in the present statute as a license to judicially devise a uniform time limitation for §301 suits.

Auto Workers v. Hoosier Cardinal Corp., 383 U.S. 696, 704 (1966) (emphasis added). Neither did the Seventh Circuit have any such license to amend §10(b) judicially. The acquiescence of Congress and principles of *stare decisis* require reversal of the decision below.

D.

The Decision Below Conflicts With Applicable Decisions of This Court Which Apply the Well-Accepted Doctrines of Equitable Tolling and Equitable Estoppel

By applying the limitations provision of §13 of the 1933 Act, which contains a three-year statute of repose, to §10(b) claims, the decision below also conflicts with decisions of the Court applying the federal doctrines of equitable tolling and equitable estoppel. These doctrines, which are deeply rooted in federal law, hold that it is against equity and good conscience to permit a person to profit by his own wrongdoing, *i.e.*, active fraudulent concealment. The district court found that Petitioner had pleaded facts entitling her to the benefit of federal equitable tolling. App. A-25. The approach of the Seventh Circuit renders those facts irrelevant and allows defendants in §10(b) cases to profit by concealment of their wrongdoing.

This Court's decisions regularly apply the federal doctrine of equitable tolling to other statutes. For example, in *Holmberg v. Armbrecht*, 327 U.S. 392 (1946), the Court held:

> [F]raudulent conduct on the part of the defendant may have prevented the plaintiff from being diligent and may make it unfair to bar appeal to equity because of mere lapse of time.

> Equity will not lend itself to such fraud and historically has relieved from it. . . . [W]here a plaintiff has been injured by fraud and "remains in ignorance of it and without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, . . ."
>
> *This equitable doctrine is read into every federal statute of limitation.*

327 U.S. at 396-97 (citations omitted; emphasis added).

This doctrine is not limited to suits in equity.[8]

> To hold that by concealing a fraud, or by committing a fraud in a manner that it concealed itself until such time as the party committing the fraud could plead the statute of limitations to protect it, is to make the law which was designed to prevent fraud the means by which it is made successful and secure. And we see no reason why this principle should not be applicable to suits tried on the common-law side of the court's calendar as to those on the equity side.

Bailey v. Glover, 88 U.S. (21 Wall.) 342, 349 (1875); *see Exploration Co. v. United States*, 247 U.S. 435 (1918). The decision below conflicts with these cases by borrowing a statute of limitations which contains a statute of repose and which therefore eviscerates the federal doctrine of equitable tolling.

The cases relied upon by the Seventh Circuit — *Agency Holding, DelCostello* and cases cited therein — do not support its result because these decisions do not borrow federal statutes containing statutes of repose. For example, in *Agency Holding*, the Court applied the four-year statute contained in the Clayton

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[8] Petitioner pleaded both legal and equitable causes of action under §10(b). Count I is at law, for damages, while Count V, in equity, is for rescission.

Act, 15 U.S.C. §15b, to actions under RICO. The Clayton Act provision does not include any statute of repose. There was no federal equitable tolling issue before the Court in *Agency Holding* because suit had been filed within the four years. *Agency Holding* and the other cases cited by the Seventh Circuit simply do not stand for the proposition that the federal courts should borrow statutes of limitations *and* repose provisions.

The Court has also consistently held that a defendant may be estopped to plead the statute of limitations where defendant's conduct has induced the plaintiff to refrain from filing suit and where defendant's assurances have lulled the plaintiff into a false security. *E.g., Schroeder v. Young*, 161 U.S. 334 (1896).

> To decide the case we need look no further than the maxim that no man may take advantage of his own wrong. Deeply rooted in our jurisprudence this principle has been applied in many diverse classes of cases by both law and equity courts and has frequently been employed to bar inequitable reliance on statutes of limitations.

Glus v. Brooklyn Eastern District Terminal, 359 U.S. 231, 232-33 (1959) (footnote omitted). The decision below would uproot these basic principles of fairness, and it produces an unfair result. Marian Short relied on and trusted her brother, Homer Weidmann. He had total control over her finances and held her power of attorney. Consequently, she did not and could not discover the Respondents' wrongdoing until 1988. The Seventh Circuit's decision casts aside the federal doctrines of equitable tolling and estoppel, which have long been applied to §10(b) cases by the lower federal courts, in favor of a rule which severely restricts the time to bring suit and which rewards fraud. Any such amendment to §10(b) should be enacted legislatively, not judicially.

This is another area in which Congress, by its silence, has acquiesced in decisions of the lower federal courts. Nearly every other circuit has held that while the court borrows the state-law

limitations period, the issue of when the period begins to run is governed by the federal law of equitable tolling. *See* cases cited at p. 11, *supra*. Indeed, the Seventh Circuit had previously so held. *See Cange v. Stotler & Co.*, 826 F.2d 581 (7th Cir. 1987). Once again, because Congress has not seen fit to change the law, it must be presumed that it does not disagree with this nearly uniform interpretation of §10(b). *See* Argument, part II, C., *supra*.

CONCLUSION

The decision below, in a marked departure from settled law in the Seventh Circuit and elsewhere, compounds the conflict among the circuits regarding the statute of limitations and tolling principles applicable to §10(b) cases. It does so in a way which would, if followed by other lower federal courts, dramatically rewrite the law of borrowing. In light of the conflict among the circuits, prior decisions of the Court, the significance of the questions presented, the acquiescence of Congress in existing law, and the disregard of principles of *stare decisis* by the court below, Petitioner respectfully submits that this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 89-3271

Marian W. Short,
Plaintiff-Appellant,

v.

Belleville Shoe Manufacturing Company, *et al.*,
Defendants-Appellees.

Appeal from the United States District Court
for the Southern District of Illinois, Alton Division.
No. 89-5061—**William L. Beatty,** *Judge.*

Argued June 12, 1990—Decided July 30, 1990

Before Posner, Easterbrook, and Manion, *Circuit Judges.*

Easterbrook, *Circuit Judge.* Belleville Shoe Manufacturing Company redeemed 550 shares of its stock from Marian Short in 1977, paying $273 per share. Twelve years later Short filed this suit under §10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and the SEC's Rule 10b-5, 17 C.F.R. §240.10b-5, contending that Belleville (a closely-held, family corporation) and its controlling shareholders had defrauded her about the value of the shares. They painted a gloomy picture of the firm's prospects in 1977; it has prospered since. Short depicts her brother Homer Weidmann, an officer of Belleville,

as her principal business adviser and contends that she delayed filing suit because Weidmann repeatedly assured her that she had received a fair price in 1977.

The district court dismissed the case under Fed. R. Civ. P. 12(b)(6), concluding that Short could not escape the statute of limitations. Short relies on state and federal tolling rules. Defendants respond that we should not inquire into tolling because §13 of the '33 Act, 15 U.S.C. §77m, which they ask us to apply, sets three years as an unyielding limit. Defendants ask, in other words, that we cease looking to state law as a source of periods of limitations in securities cases, on the authority of *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), which applied a federal statute of limitations (from the antitrust laws) to cases under the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §§1961-68.

I

A

For many years we have applied to cases under Rule 10b-5 statutes of limitations borrowed from state blue sky statutes, adding an overlay of tolling principles from state and federal law. *Davenport v. A.C. Davenport & Son Co.*, 903 F.2d 1139 (7th Cir. 1990), is the most recent in a line going back at least to *Parrent v. Midwest Rug Mills, Inc.*, 455 F.2d 123, 125-27 (7th Cir. 1972). See also, e.g., *Norris v. Wirtz*, 818 F.2d 1329 (7th Cir. 1987); *Teamsters Local 282 Pension Trust Fund v. Angelos*, 815 F.2d 452 (7th Cir. 1987); *Suslick v. Rothschild Securities Corp.*, 741 F.2d 1000 (7th Cir. 1984); *Goldstandt v. Bear, Stearns & Co.*, 522 F.2d 1265 (7th Cir. 1975); *Tomera v. Galt*, 511 F.2d 504 (7th Cir. 1975). Like the other courts of appeals, we looked to state law because Congress has not enacted a statute of limitations for Rule 10b-5, and could hardly have been expected to—for the right of action under Rule 10b-5 was

created by the courts rather than Congress. Section 10(b) itself grants rulemaking authority to the SEC; because it does not create a right of action, it is not accompanied by a statute of limitations.

Because Congress was silent, we applied the principle, derived from the Rules of Decision Act, 28 U.S.C. §1652, that when federal law is deficient, state law fills the gap. One of the venerable applications is to obtain periods of limitations from state law. E.g., *Auto Workers v. Hoosier Cardinal Corp.*, 383 U.S. 696, 704 (1966) (collecting cases). This is so predictable that Congress may anticipate it, so that when it does not enact a federal statute of limitations it means to leave in place the background rule that state law applies. See *Reed v. United Transportation Union*, 109 S. Ct. 621, 625 (1989); *Agency Holding*, 483 U.S. at 147; *DelCostello v. Teamsters*, 462 U.S. 151, 158 (1983). Federal courts are so accustomed to turning to state periods of limitations that we (and our colleagues in other circuits) did this on auto-pilot, without discussing whether something differentiated securities laws from other statutes. See also *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 210 n.29 (1976); *Herman & MacLean v. Huddleston*, 459 U.S. 375, 384 n.18 (1983), both recognizing the prevailing practice.

Yet there are differences. One is that Congress could hardly have anticipated that courts would turn to state law for a period of limitations, when Congress did not create the right of action in the first place. We are not dealing here with a problem of deciding whether Congress meant to *depart* from a norm; we have a problem of the courts' creation. See *United Parcel Service, Inc. v. Mitchell*, 451 U.S. 56, 68 n.4 (1981) (Stewart, J., concurring); *DelCostello*, 462 U.S. at 158-59 n.12. Federal courts have an obligation to create stable periods of limitations for their handiwork. *Smith v. Chicago*, 769 F.2d 408 (7th Cir. 1985).

A second difference is that Congress has not been silent. The securities acts are jammed with statutes of limitations. For every

statutory right of action there is a corresponding statute of limitations. The Securities Act of 1933 gave the purchaser two years from the date of discovering the fraud, but in no event more than ten years from the date of sale. 48 Stat. 84 (1933). When Congress enacted the '34 Act, it amended this statute (now §13 of the '33 Act) and added four more, one for each of the new express rights of action. See §§9(e), 16(b), 18(c), and 29(b), 15 U.S.C. §§78i(e), 78p(b), 78r(c), and 78cc(b). In 1988 it added another for inside trading cases, 102 Stat. 4680-81, to be codified as §20A, 15 U.S.C. §78t-1. There can be no presumption that Congress meant courts to look to state law, when every time Congress has authorized a federal remedy it has also created a federal period of limitations.

Third, turning to state law for periods of limitations creates special problems under the securities acts because the acts do not apply in the first place unless the transactions occurred in interstate commerce. At least two state statutes therefore could be applied to any case. Courts must use conflict-of-laws principles to pare the number down to one. Congress enacted a national rule against fraud because it believed that national law ought to govern multi-state transactions. Returning to state law to fetch a period of limitations is inconsistent in spirit with this decision.

All of this would be by the by if the Rules of Decision Act *requires* federal courts to use state law. But two cases decided after the courts of appeals began to apply state law under Rule 10b-5 hold that it does not. *DelCostello* concluded that a six-month period drawn from the National Labor Relations Act governs "hybrid" suits alleging an employer's breach of contract coupled with a union's breach of the duty of fair representation. *Agency Holding* decided to apply the four-year period of limitations in the antitrust laws to suits under RICO. These cases call for fresh examination of the question whether to turn to state law in securities cases. The third circuit conducted such an examination and concluded that §13 of the '33 Act is the appropriate statute. *In re Data Access Systems Securities Litiga-*

tion, 843 F.2d 1537 (3d Cir. 1988) (in banc). The Securities and Exchange Commission likewise believes that federal law supplies the period of limitations, although it thinks that the new §20A rather than §13 is the closer match. Brief for the United States as Amicus Curiae in *Lebman v. Aktiebolaget Electrolux,* No. 88-1144 (October Term, 1988), *cert. denied,* 109 S. Ct. 3214 (1989). The time is ripe for reconsideration in this circuit too.

"[W]hen a rule from elsewhere in federal law clearly provides a closer analogy than available state statutes and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking", *DelCostello,* 462 U.S. at 171-72, quoted in *Agency Holding,* 483 U.S. at 148, it is appropriate to select a federal statute of limitations. Securities law satisfies both branches. The statutes of limitations in the securities acts are addressed to the conduct at stake in this case—securities fraud. Section 13, in particular, covers the express right of action in §12, which concerns incorrect statements and material omissions in the course of selling securities. Congress has spoken directly to the appropriate statute of limitations for litigation of the sort Short presses. When the statute contains not only a statute of limitations for every express right of action, but also an express right of action quite similar to the implied right of action, then the federal statute "clearly provides a closer analogy than available state statutes".

Difficulties in selecting an appropriate state statute also influence the "practicalities of litigation". Even when turning to state law, courts should endeavor to find a single period of limitations "that can be applied with ease and predictability in all 50 States." *Owens v. Okure,* 109 S. Ct. 573, 578 (1989). That task has proved daunting in securities cases. Different courts have looked to different bodies of state law for inspiration. Some borrow from the statute generally applicable to fraud; some borrow from state blue sky laws; some courts use a little of each, depending on the particulars of the claim under

Rule 10b-5. The ABA's Committee on Federal Regulation of Securities, *Report of the Task Force on Statute of Limitations for Implied Action,* 41 Bus. Law. 645, 659-66 (1986), collects the decisions from around the circuits. Some states have more than one fraud or blue sky statute, complicating matters. States also revamp their laws more frequently than Congress amends the Securities Exchange Act. Illinois, for example, amended the statute of limitations in its blue sky act in 1985, and one of the questions with which the district court wrestled is the extent to which the alterations apply to a claim that accrued in 1977. (The district judge, disagreeing with four other district judges in the circuit, concluded that Short had at most two years after January 1, 1986, the effective date of the amendment. See also *Davenport,* 903 F.2d at 1141 n.5; *Norris,* 818 F.2d at 1333 n.*.) Translating state periods of limitations to federal court also has led to difficult questions concerning whose tolling and estoppel doctrines apply: the state's, the federal court's, or both? *Davenport, Norris,* and many other cases grapple at length with the interaction of state and federal tolling rules.

Although this circuit regularly uses state blue sky laws, other circuits have been equally committed to different courses. From the perspective of practitioners litigating cases originating in many states (especially class actions), the situation is a nightmare. Lawyers and courts alike devote untold hours to identifying proper state analogies and applying multiple (conflicting or cumulative) tolling doctrines. "This uncertainty and lack of uniformity promote forum shopping by plaintiffs and result in wholly unjustified disparities in the rights of different parties litigating identical claims in different states. Neither plaintiffs nor defendants can determine their rights with any certainty. Vast amounts of judicial time and attorneys' fees are wasted." ABA Committee, 41 Bus. Law. at 647. Loud calls for reform issue from scholars and the bar. With a unanimity unmatched in any other corner of securities law, everyone wants a simpler way—and to everyone that means a uniform federal statute of limitations. In addition to the ABA Committee's

plaint, see, e.g., Thomas Lee Hazen, 2 *The Law of Securities Regulation* §13.8 (2d ed. 1990); Bateman & Keith, *Statutes of Limitations Applicable to Private Actions Under SEC Rule 10b-5: Complexity in Need of Reform,* 39 Mo. L. Rev. 165, 183 (1974); Ruder & Cross, *Limitations on Civil Liability Under Rule 10b-5,* 1972 Duke L.J. 1125, 1142; Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion,* 13 Wayne L. Rev. 637 (1967); Note, *Statutes of Limitation for Rule 10b-5,* 39 Wash. & Lee L. Rev. 1021 (1982). As Professor Loss puts it, *Fundamentals of Securities Regulation* 1168-69 (1983): "This reference to state law makes for a great amount of utterly wasteful litigation. . . . Would it not be eminently more consistent with the overall statutory scheme to look to what Congress itself did when it was thinking specifically of private actions in securities cases than to a grab-bag of more or less analogous state statutes?"

Norris examined this subject and concluded that the statute of limitations in §13 fits actions under Rule 10b-5 far more closely than the collection of statutes absorbed from state law. 818 F.2d at 1332-33. We did not jettison our existing approach, however, deeming it "too late for an inferior federal court to turn back the clock", 818 F.2d at 1333. When we decided *Norris,* the courts of appeals were unanimous in thinking that state law supplies the statutes of limitations under Rule 10b-5. A month later the Supreme Court decided *Agency Holding.* Six months after that the third circuit broke ranks in *Data Access,* relying on *Agency Holding* and the analysis in *Norris.* Now that there is an established conflict among the circuits and the SEC has endorsed the use of federal law, we need not be so meek. Although *stare decisis* has its claims, *Agency Holding* took a bold step that invites the inferior federal courts to reconsider their handling of adjacent fields. We hold that federal and not

state law supplies the statute of limitations in suits under §10(b) and Rule 10b-5.*

We leave for the future all questions concerning retroactive application of this decision. Retroactivity has not been briefed, and the retroactive application of decisions affecting periods of limitations is a question of some subtlety depending on the nature of reliance interests. See *Chevron Oil Co. v. Huson,* 404 U.S. 97 (1971); *St. Francis College v. Al-Khazraji,* 481 U.S. 604 (1987); *Goodman v. Lukens Steel Corp.,* 482 U.S. 656, 662-64 (1987); *Hill v. Equitable Trust Co.,* 851 F.2d 691 (3d Cir. 1988) (applying *Data Access* retroactively); cf. *American Trucking Ass'ns, Inc. v. Smith,* 110 S. Ct. 2323, 2343-45 (Scalia, J., concurring), 2347-52 (Stevens, J., dissenting) (1990). It is enough for the moment to observe that new rules of law apply in the cases that establish them and that Short cannot have relied on Illinois law, because she claims to have been unaware of the basis for litigation until a short time before filing suit. Effects of reliance on our former holdings may be determined when the plaintiff demonstrates reliance.

B

Federal securities laws contain two candidate statutes of limitations. The first is §13 of the Securities Act of 1933, as amended by the Securities Exchange Act of 1934, which provides:

> No action shall be maintained to enforce any liability under section 11 or section 12(2) unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made

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* Because this decision changes a rule of law established in this circuit, effectively overruling cases that borrowed periods of limitations from state law, it was circulated to all judges in regular active service. See Circuit Rule 40(f). No judge voted to hear the case in banc.

> by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 12(1), unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under section 11 or section 12(1) more than three years after the security was bona fide offered to the public, or under section 12(2) more than three years after the sale.

Section 11 deals with errors and omissions in registration statements, including the portion of the registration statement that circulates as the prospectus. Section 12(1) deals with sales "in violation of section 5"—that is, unregistered sales of securities required to be registered. Section 12(2) addresses all other forms of materially incorrect or misleading selling literature and oral communications in the sale of a security. Data Access selected §13 as the appropriate federal law because misstatements and omissions that violate §12(2) are the closest match to the subjects of Rule 10b-5. (Short could not have sued under §12 itself; she complains of fraud by the buyer, while §12(2) is addressed to fraud by the seller. Still, §12(2) applies to the kind of conduct involved here.)

The second candidate is §20A(b)(4) of the Securities Exchange Act of 1934, added by the Insider Trading and Securities Fraud Enforcement Act of 1988. This provides:

> No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

Section 20A(a) defines "the subject" as violating the '34 Act or its rules "by purchasing or selling a security while in possession of material, nonpublic information". The Solicitor General, representing the SEC in *Lebman,* asked the Supreme Court to use this statute for all actions under Rule 10b-5, on the rationale that inside trading violates Rule 10b-5, so that employing §20A(b)(4) just extends it from some to all Rule 10b-5 actions.

Choosing between these statutes is difficult. Section 13 is attractive because it covers §12(2), which describes the offense to which Rule 10b-5 is applied: fraudulent misstatements or omissions in connection with the purchase or sale of securities. Rule 10b-5 came into being when §13 was the only game in town. Any court choosing a federal statute of limitations between 1946 (the date of the first decision recognizing a private right of action under Rule 10b-5) and 1988 necessarily would have selected §13. It is also the statute *Data Access* picked. To pick §20A would be to create a fresh conflict among the circuits. Because a principal reason for choosing a federal law is to replace confusion with certainty, we are reluctant to depart from the statute that will be employed in the third circuit.

On behalf of §20A one may say that five years represents Congress' latest thoughts and that because trading on material inside information violates Rule 10b-5, the *only* way to apply a single statute of limitations to all actions under that Rule is to use §20A(b)(4). Clever lawyers could describe even a garden variety fraud as "purchasing or selling a security while in possession of material, nonpublic information"—that is, the truth—blurring the line betwen the offenses and making the choice of a period of limitations difficult. Moreover, §20A offers plaintiffs more time than does §13. Section 10(b) and Rule 10b-5 require the plaintiff to prove scienter, which a plaintiff under §12(2) need not; perhaps the additional years are appropriate to the extra requirements of litigation under Rule 10b-5.

Interests in uniformity tug both ways: if we choose §20A we shall have one statute of limitations for all Rule 10b-5 cases in the seventh circuit, but different rules in the seventh and third circuits. If we choose §13 we shall be in line with the third circuit, but different kinds of claims under Rule 10b-5 will be subject to different periods of limitations. The latter diversity is likely to be tolerable. To obtain the five-year period of §20A, the plaintiff would have to sue under §20A, establish trading by an in-

sider (Belleville Shoe's insiders did not trade with Short), and accept the limitations of that statute, including the restriction of damages to the defendants' profit (as opposed to the plaintiff's loss). In the great bulk of cases, there will be no ambiguity.

One interest cuts strongly in favor of §13: it is a statute of repose, while §20A appears to be a statute of limitations. Section 13 gives one year from discovery, but "*[i]n no event* shall any such action be brought to enforce a liability created . . . under section 12(2) more than three years after the sale." (Emphasis added.) Conduct by the defendant that postpones the date of discovery therefore does not extend the period of suit by more than two years. *Data Access* concluded that equitable tolling does not postpone the accrual of the claim, or equitable estoppel does not bar the invocation of §13. See also *Admiralty Fund v. Hugh Johnson & Co.*, 677 F.2d 1301, 1308 (9th Cir. 1982); *Sumner v. Land & Leisure, Inc.*, 664 F.2d 965 (5th Cir. 1981); Bloomenthal, *Statutes of Limitations and the Securities Acts—Part I*, 7 Sec. & Fed. Corp. L. Rep. 18, 21 (1985) (collecting legislative history); ABA Committee, 41 Bus. Law. at 655. Cf. *Darms v. McCulloch Oil Corp.*, 720 F.2d 490 (8th Cir. 1983); *Aldrich v. McCulloch Properties, Inc.*, 627 F.2d 1036 (10th Cir. 1980) (both interpreting language in other statutes identical to §13 as precluding any extension beyond three years).

Courts say that equitable tolling does not apply under §13, see Hazen, 1 *Law of Securities Regulation* §7.5.4 at 340-42 (collecting cases), but this is not strictly accurate. It is better to say that equitable tolling and related doctrines do not extend the period of limitations by more than the two-year grace period §13 allows. *Norris*, 818 F.2d at 1332. Congress did not obliterate these valuable doctrines so much as it set bounds on the length of delay. It may be that equitable estoppel could preclude resort to the one-year period after discovery, even though no tolling of the three-year outer limit is possible; we need not decide. Unless the "in no event more than three" language cuts off claims of tolling and estoppel at three years, however, it serves no purpose

at all—what other function could be served by such language in a statute that starts the time on discovery?

Section 20A, by contrast, appears to be an ordinary statute of limitations. The SEC believes that it is a statute of repose as well as a statute of limitations, see *Lebman* amicus brief at 14 n.17, but it is not so clear to us. The language is in the traditional form of a statute of limitations, and the Solicitor General did not cite any legislative history indicating that it is more potent than the usual variety. (No case has been decided under the period of limitations established in §20A, and none is likely to be until after 1993.)

The difference between statutes of limitations and statutes of repose is substantial in securities litigation. Indeed, the SEC's submission that §20A should be used across the board appeared to depend on its conclusion that §20A, like §13, is a statute of repose. All of the express provisions in the '33 and '34 Acts (other than §20A), are drawn as statutes of repose, and deliberately so. Prices of securities are volatile. If suit may be postponed indefinitely on equitable grounds, then investors may gamble with other people's money. An investor in Short's position may sell her shares for a price certain. If the firm does poorly, she keeps the money; if it does well, she sues and asks for the increase in value. Congress chose one year after discovery, and a cap of two additional years on tolling principles, in order to curtail the extent to which the securities laws permit recoveries based on the wisdom given by hindsight. This was why in 1934 Congress repealed the period in the original version of the '33 Act (two years from discovery, and in no event more than ten) and replaced it with the current §13 (one year from discovery, and in no event more than three). See H.R. Conf. Rep. No. 1838, 73d Cong., 2d Sess. 32, 36, 42 (1934); 78 Cong. Rec. 8198-8203 (May 7, 1934) (Senate amendments carried to the conference); J.S. Ellenberger & Ellen P. Mahar, 6 *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934* 6565-66, 6718, 6993 (1973), and

7 *id.* at 7743-44. Investors then have a more powerful incentive to investigate rather than accept another person's word without question, as Short says she did. Prudent investors almost always can sniff out fraud (or enough smoke to justify litigation) within three years. Section 13 cuts off only the claims of the most trusting or somnolent—or the most wily, those who wanted to wait as long as possible.

Setting an outer limit for claiming fraud or material omissions in the sale of securities is an important aspect of §13, one of the principal reasons Congress designed the statute that way. Section 20A, by contrast, uses for inside trading cases a measure of damages that the passage of time does not affect. Section 20A(b)(1) provides that the "total amount of damages . . . shall not exceed the [insider's] profit gained or loss avoided in the transaction or transactions that are the subject of the violation." Profit gained or loss avoided is a contemporaneous measure: the difference between the price the insider realizes and the market price of the securities after the news is released. *Wisconsin Real Estate Investment Trust v. Weinstein,* 781 F.2d 589, 596-97 (7th Cir. 1986); *SEC v. MacDonald,* 699 F.2d 47, 52-55 (1st Cir. 1983) (in banc); *Gerstle v. Gamble-Skogmo, Inc.,* 478 F.2d 1281, 1306 n.27 (2d Cir. 1973) (Friendly, J.). This sum is fixed within days after the trading, sometimes within hours. No one has a free put or call of securities; no one can use delay in bringing suit to speculate on the firm's future prosperity. Section 20A may use a five-year period, and be drafted as an ordinary statute of limitations, precisely because the reasons for setting the shorter one-and-three period for fraud are not present. To select §20A(b)(4) as the rule for *all* Rule 10b-5 actions, just because a five-year period has been deemed appropriate for one atypical kind of violation, would let the tail wag the dog. Congress did not say that §20A applies to all cases under Rule 10b-5; it did not amend §13; it limited the scope of §20A's statute of limitations to a particular and atypical kind of violation. Section 20A(b)(4) has been prescribed for inside trading cases; run-of-the-mine frauds under Rule 10b-5 should be

governed by the statute in force when Rule 10b-5 came into being, the statute *designed for* the kind of conduct about which Short and most other 10b-5 plaintiffs complain: §13 of the Securities Act of 1933.

Application of §13 to this case is straightforward. Short sold her shares to Belleville Shoe on May 5, 1977. Although she contends that she did not discover the fraud until late 1988, the second sentence of §13 sets three years after the sale as the outer limit for litigation. That time expired in 1980. Suit was not filed until 1989. It is untimely.

II

Short's second federal claim arises under RICO. She contends that Belleville and the other defendants carried out a pattern of racketeering acts (that is, of securities fraud) by acquiring the stock of four minority investors in 1977. Short, Louise Lampert Larsen, and Jean Lampert Sundheim sold their stock in spring 1977, and Rosalind Wagner that fall. These sales, according to Short, establish a "pattern" of fraud characterized by the necessary "continuity plus relationship", *H.J. Inc. v. Northwestern Bell Telephone Co.*, 109 S. Ct. 2893, 2900 (1989). The district court disagreed, holding that four transactions in close proximity 12 years ago do not establish the "continuity" element in the absence of a threat of enduring fraud.

We approach the question with diffidence, because "continuity plus relationship" is such an ambulatory phrase. Still, it it impossible to stretch the events of 1977 into a "pattern" of fraud. Belleville Shoe's board of directors authorized the purchases at a price of $273 per share in a single resolution, dated May 1, 1977. The four investors accepted Belleville Shoe's offer at different times—Wagner accepting in the fall because she was out of the country when the other three said yes. One offer followed by four acceptances hardly threatens "continuity" of any kind. The Court said in *H.J.* that "[p]redicate acts extending over a few weeks or months and threatening no future

criminal conduct do not satisfy this [continuity] requirement." 109 S.Ct. at 2902. This language supplied the basis of the holding in *Sutherland v. O'Malley,* 882 F.2d 1196 (7th Cir. 1989), that a course of conduct stretching over five months did not amount to "continuity". See also *Management Computer Services, Inc. v. Hawkins, Ash, Baptie & Co.,* 883 F.2d 48 (7th Cir. 1989).

Short tries to rescue her case by characterizing the threat of further misconduct against minority shareholders as the source of continuity. She does not identify any such investors, however, or explain how they were threatened. The complaint does not mention any further purchases of stock under circumstances suggesting fraud. RICO is not designed to transfer to federal court all claims of oppression of minority investors in violation of fiduciary duties established by corporate law. Short may pursue such contentions in state court; all of her claims under state law were properly dismissed, for lack of an independent jurisdictional basis, following the failure of her two federal claims. Short insists that Illinois' tolling rules would allow her to recover from Belleville Shoe and her relatives 13 years after the events. She may test that belief in the appropriate forum.

Affirmed

POSNER, *Circuit Judge,* concurring. I have no disagreement with the court's opinion or judgment, and join both, writing separately only to express reservations about the principle of "borrowing" a period of limitations from one statute for use with another (here, a rule of the SEC, but the principle is the same) that has none. The Supreme Court's unwavering attachment to the principle leaves us no choice but to apply it, but that attachment is beginning to be questioned, *Agency Holding Corp. v. Malley-Duff & Associates, Inc.,* 483 U.S. 143, 157-70 (1987) (concurring opinion), and I would like to add my small voice to the chorus.

Borrowing a period of limitations from one statute to use with another that doesn't have its own limitations provision is a matter of which round peg to stuff in a square hole. It artificially truncates the court's choice of an *appropriate* period, one well suited to the *particular* statute under consideration. It also runs the risk of applying one unprincipled legislative deal to a problem entirely outside the scope of the deal. Suppose Statute A specifies no period of limitations. Statute B regulates analogous conduct, and has a six-month period. But maybe B has such a short deadline for suit only because the interest group that opposed the enactment of B had enough muscle to block a longer deadline that would have made more sense from a neutral standpoint. In that event, to borrow B's limitations period for use with A will project the interest-group pressures that deformed B into a completely new area of conduct.

Whether or not courts are aware of this danger, they do attempt to correct for it by considering, as part of the borrowing procedure, the suitability to the substantive rule under consideration of the limitations periods in the various candidate statutes of limitations. But this places a lot of balls in the air. The considerations bearing on the suitability of one limitations period over another include the difficulty of investigating potential violations, the possibility that the consequences of wrongdoing will be delayed, the opportunities for wrongdoers to conceal the wrong, the rate at which evidence of wrongdoing and also evidence pertinent to the alleged wrongdoer's defenses is likely to decay, the sophistication of the relevant tribunals in handling stale evidence, the desirability of freeing court time for fresh claims, the interest of potential defendants in repose—that is, in knowing after a definite period has passed that they no longer have to worry about being sued—and the effect on the deterrence of statutory violators of reducing the time for bringing suit. When these considerations are mingled with the underlying question of the similarity between the conduct in the case at issue and the conduct to which the various candidate statutes of

limitations apply, we have the essential condition for standardless, discretionary judgment: a multi-factor test with no weights on the factors. Since courts cannot be expected to converge on a uniform outcome when they are operating under such a standard, predicting what statute of limitations will be borrowed is impossible and as a result extensive litigation often is necessary before a definitive conclusion on the limitations period emerges. It may not come until a Supreme Court decision is rendered resolving an intercircuit conflict that was years in the brewing.

As we noted in *Hemmings v. Barian,* 822 F.2d 688, 689 (7th Cir. 1987), judges feel that they have to borrow an existing statute of limitations rather than lay down a period of limitations as a matter of federal common law because it would be arbitrary to pick a term of years. They feel in other words that enactment of a limitations period, because of its inescapable arbitrariness, is a legislative rather than a judicial task. Legislators can be as arbitrary as they please within the broad limits set by the Constitution but judges are supposed to reason to their conclusions, and how can you *reason* to 3 years over 2, 300 days over 240, 20 years over 15? You cannot; but neither can you reason to the right statute of limitations to borrow. The imponderables are so numerous that in the end the borrowing judgment, too, is inescapably arbitrary, as the present case illustrates.

What is to be done? There are several possibilities. One would be for courts to drop the mask and create statutes of limitations for claims that lack them. There is precedent for this in the judicial doctrine of laches, which on at least one occasion was firmed up into a period of definite length. *Smith v. City of Chicago,* 769 F.2d 408 (7th Cir. 1985). Yet even then we borrowed the limitations period in an existing statute. The difficulty with creating a statute of limitations *ex nihilo* lies in the fact that judge-made rules come in the first instance from the bottom of the judicial hierarchy, rather than being imposed from on high. In the early days of a new substantive statute that

specified no limitations period, each district judge would be selecting a period of limitations for the individual case, each court of appeals would be selecting the period for the cases in the circuit, and only when the Supreme Court got a case would the definitive period finally be declared. The improvements over the borrowing procedure would be modest; they would be chiefly in the area of judicial candor.

An institutional solution is necessary, and two possibilities come to mind. One, which wouldn't work in this case because the cause of action postdates the enactment of the statute under which it arises, would be for Congress to adopt a rule that every statute shall contain a statute of limitations. This course would be superior to Congress' adopting (as sometimes proposed) a general catch-all statute of limitations, because there is no single period of limitations that would be suitable for the entire range of causes of action in statutes that do not specify a period. Such a rule might, it is true, be ineffectual without a nagging agency within Congress to enforce it, some counterpart to the Congressional Budget Office, as proposed in the Report of the Federal Courts Study Committee 21-22, 89-93 (April 2, 1990)—unless the Supreme Court adopted Justice Scalia's view that if a statute contains no period of limitations, there just is no deadline on suing. *Agency Holding Corp. v. Malley-Duff & Associates, Inc., supra,* 483 U.S. at 164. This would cause considerable havoc but could be mitigated by a rule (well within the power of judges to create, I believe) that, in the absence of a statutory limitations period, the courts will apply the equitable doctrine of laches even if the cause of action is legal rather than equitable. Then the defendant could defend by showing that the plaintiff had unreasonably delayed in bringing the suit and that the defendant had been hurt by the delay. There is precedent for applying laches in cases at law. *Piper Aircraft Corp. v. Wag-Aero, Inc.,* 741 F.2d 925, 939 (7th Cir. 1984) (concurring opinion).

The second institutional possibility would be for Congress to delegate to the Judicial Conference of the United States, or to

some new agency modeled on the Sentencing Commission—perhaps my hypothetical "nagging agency"—the power to adopt by regulation a period of limitations for any statute that does not have one. This would lift the burden from Congress of having to specify a limitations period in every enactment and would shift it to an expert body that could avoid the delay of litigation. It would be a great improvement over borrowing.

A true Copy:

Teste:

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Clerk of the United States Court of Appeals for the Seventh Circuit

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS

NO. 89 5061

MARIAN W. SHORT,
Plaintiff,

vs.

BELLEVILLE SHOE MANUFACTURING COMPANY,
et al.,
Defendants.

ORDER

This matter is before the court on the defendants' Motion to Dismiss Plaintiff's Amended Complaint. The defendants urge the court to dismiss the amended complaint based upon various legal theories, all of which merit discussion.

FACTS AND BACKGROUND

The plaintiff filed her original complaint on February 16, 1989. An amended complaint was filed on April 20, 1989. The amended complaint alleges that on May 5, 1977, the plaintiff and Belleville Shoe entered into a redemption agreement wherein Belleville Shoe redeemed all 550 shares of Belleville Shoe stock owned by the plaintiff. This redemption transaction, according to the plaintiff, was in violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 in that the individual defendants and Belleville Shoe employed devices, schemes and artifices to defraud; made untrue statements of material facts and omitted to state material facts; and/or engaged in acts, practices and a course of business which operated as a fraud or deceit upon the plaintiff. In support of these allegations. the plaintiff further alleges that the redemption price of

$273.00 per share of stock was significantly less than the fair value of the stock, and that the redemption price was based upon the amount of money needed by the plaintiff at the time, rather than the actual fair value of the stock. Allegedly, the false representations and concealed material facts were not discovered until the records of Belleville Shoe were examined by her attorney on October 4, 1988. The reason for the delay, according to the complaint, is that the plaintiff had continued confidence and trust in the defendants, who happened to be members of her family, and that her brother, defendant Homer Wideman, operated as plaintiff's business confident, adviser and pursuant to a power of attorney which plaintiff had executed in his favor.

The complaint further alleges that the defendants violated 18 U.S.C. §§1962(b), (c) and (d), (RICO) through a pattern of racketeering activity in that the defendants sought to, and did, redeem all the shares of Belleville Shoe stock from the minority stockholders through fraudulent representations and omissions.

Finally, the amended complaint seeks damages for common law claims of fraud, rescission, constructive trust, and breach of fiduciary relationship, based upon the above-described redemption transaction.

SECURITIES ACT OF 1934 AND RULE 10b-5

Counts I and V of the plaintiff's amended complaint allege violations of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j (b) and Rule 10b-5, 17 C.F.R. 240.10b-5. The defendants seek to have these counts dismissed on the grounds that the actions are barred by the applicable statute of limitations. The statute of limitations to be applied in a federal securities law claim in Illinois is the Illinois Securities limitation period provided in Ill. Rev. Stat. Ch. 121½, ¶137.13D. *Teamsters Local 282 Pension Trust Fund v. Angeles,* 815 F.2d 452, 455 (7th Cir. 1987), and cases cited therein. Paragraph 137.13D, effective January 1, 1986, provides:

> No action shall be brought for relief under this Section or upon or because of any of the matters for which relief is granted by this Section after three years from the date of sale, provided, that if the party bringing the action neither knew nor in the exercise of reasonable diligence should have known of any alleged violation . . . which is the basis for the action, the three-year period provided herein shall begin to run upon the earlier of (1) the date upon which the party bringing such action has actual knowledge of the alleged violation of this Act, or (2) the date upon which the party bringing such action has notice of facts which in the exercise of a reasonable diligence would lead to actual knowledge of the alleged violation of this Act; but in no event shall the period of limitation so extended be more than two years beyond the expiration of the three-year period otherwise applicable.

Ill. Rev. Stat. Ch. 121½, ¶137.13D, as amended January 1, 1986.

The plaintiff does not dispute that Paragraph 137.13D is the applicable statute of limitations to be applied. Plaintiff argues however, that in federal securities actions, the federal doctrine of equitable tolling should be applied, and because she has pled facts which invoke the federal equitable tolling doctrine, the court should toll the Illinois limitation period, thereby disregarding the two year repose provision provided in 137.13D.

Prior to January 1, 1986, Paragraph 137.13D provided that no action shall be brought after three years from the date of sale. The statute was silent with respect to when the three year limitation period began to run. Accordingly, the Seventh Circuit consistently held that in the event the party could not, through the exercise of reasonable diligence, discover a violation of the Securities Act, the federal doctrine of equitable tolling should be applied to extend this three year limitation period. *Cange v. Stotler and Co., Inc.*, 826 F.2d 581, 586, n.3 (7th Cir.

1987); *Norris v. Wirtz,* 818 F.2d 1329, 1331 (7th Cir. 1987) *Cert. denied,* ____ U.S. ____, 108 S.Ct. 329; *Suslick v. Rothchild Security Corp.,* 741 F.2d 1000, 1004 (7th Cir. 1984); *Parrent v. Midwest Rug Mills, Inc.,* 455 F.2d 123, 128 (7th Cir. 1972). These decisions, however, were rendered with respect to the pre-1986 statute. Assuming, as the court must when considering a motion under Rule 12(b)(6), that the allegations in the complaint are true, and viewed in the light most favorable to the plaintiff, *Ellsworth v. City of Racine,* 774 F.2d 182, 184 (7th Cir. 1985), the plaintiff herein did not, and could not have discovered the alleged violation. Thus the statutory limitation period of ¶137.13, along with the federal equitable tolling applicable prior to the time of the amendment, had not yet expired when ¶137.13D was amended.

Under established Illinois law, "[a]n amendment to a limitation statute shortening the period within which an action must be filed will be applied retroactively to actions not as yet commenced, provided there is a reasonable time after the effective date of the amendment within which to bring the action." *Hupp v. Gray,* 73 Ill.2d 78, 83, 22 Ill. Dec. 513, 328 N.E.2d 1211 (1978). The new period can be applied without more, if under the new statute a reasonable time remains; if a reasonable time does not remain, then a reasonable time will be allowed. *Mega v. Holy Cross Hospital,* 111 Il.2d 416, 420-21, 95 Ill. Dec. 812, 490 N.E.2d 665 (1986).

With respect to the instant matter, at the time the statute of limitations was amended, i.e., January 1, 1986, the plaintiff's claim had not yet been barred. Under the amended statute of limitations, the plaintiff would have three years from the date of sale, or three years from the discoverability of the alleged violations, *but in no event more than two years beyond the original three year period* otherwise applicable. Ill. Rev. Stat. Ch. 121½, ¶137.13D, as amended. On January 1, 1986, the plaintiff would have been afforded an additional two years, under the statute, i.e., the time which shortens the period within which

the action must be filed, if this two years is reasonable. *Hupp*, 22 Ill. Dec. at 515. The legislature, through imposing an absolute bar to securities violations, has determined that two years beyond the original period of limitations is sufficient for parties bringing actions pursuant to the Illinois Securities law. Ill. Rev. Stat. Ch. 121½, ¶137.13D, even if discovery was not reasonable or subverted. See Interpretive Comments, to ¶137.13D, Fein & Sosin. The time remaining for the plaintiff to file her lawsuit from the amendment, was two years. This is the identical amount of time which the Illinois statute provides for any securities violation. Thus, the court finds that the remaining two years under the amendment to ¶137.13D is a reasonable time within which plaintiff should have brought her securities claim under §10(b) and Rule 10b-5. Since this cause of action was brought on February 16, 1989, i.e., beyond two years from January 1, 1986, the action is untimely. Accordingly, the defendants' Motion to Dismiss Counts I and V is hereby granted.[1]

RICO CLAIMS

Plaintiff has alleged certain violations under the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §1961-1968 in Counts II, III and IV. In support of these claims, plaintiff alleges that the defendants committed mail and wire fraud on the plaintiff. Allegedly, plaintiff did not discover the fraud until October, 1988. (See discussion, Supra) Furthermore, the plaintiff alleges that the defendants committed fraudulent acts upon Louise Lampert Larsen and Jean Lampert

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[1] The court recognizes that this result differs from the results reached by the District Court in the Northern District of Illinois, See *John v. Phelps*, 1989 U.S. Dist. LEXIS 6045 (N.D. Ill. 1989), *Basil v. Leidesdorf*, 1989 U.S. Dist. LEXIS 5490 (N.D. Ill. 1989), *Pucci v. Santi*, 711 F. Supp. 916 (N.D. Ill. 1989), and *Greeting v. Prizant*, 664 F. Supp. 343 (N.D. Ill. 1987), the court believes that the results reached herein is more consistent with the intent of the Illinois Legislature in enacting the amendment to ¶137.13D.

Sundheim in the Spring of 1977 and upon Rosalind Wagner in the Fall of 1977. Plaintiff alleges that the defendants considered the interests of the Lampert and Wagner stockholders to be "potentially adverse" to those of Belleville Shoe. These actions of redeeming the stock of the minority stockholders, according to plaintiff constitute a pattern of racketeering activity in violation of the RICO statute.

Initially, with respect to the RICO counts, defendants argue that these counts are barred by the applicable statute of limitations. The defendants correctly point out that the Supreme Court has recently determined that the time period within which one must file a RICO action is the four year statute of limitations provided in the Clayton Act, 15 U.S.C. §15b. *Agency Holding Corp. v. Malley-Duff and Associates,* ____ U.S. ____, 107 S.Ct. 2759, 2765, 97 L.Ed.2d 121 (1987). In that plaintiff sold her shares of Belleville Shoe stock on May 5, 1977, the defendants argue that any RICO causes of action which plaintiff may have had are now barred by the four year stautute of limitation. The plaintiff does not dispute the applicable time period for a RICO action. However, the plaintiff urges that again, the federal equitable tolling doctrine should be applied. This argument is well taken. The federal equitable tolling doctrine is read into every federal statute of limitations. *Holmberg v. Armbrecht,* 327 U.S. 392, 397, 66 S.Ct. 582, 585, 90 L.Ed. 743 (1946); *Sperry v. Barggren,* 523 F.2d 708, 710 (7th Cir. 1975).

The plaintiff has pled that the defendants actively concealed the wrongful behavior of the defendants. *Tomera v. Galt,* 511 F.2d 504, 510 (7th Cir. 1975). For the purposes of a motion to dismiss, as previously discussed, taking the allegations of the complaint in the light most favorable to the plaintiff, *Ellsworth,* 774 F.2d at 183, the plaintiff has stated facts which may give rise to the federal equitable tolling doctrine.

The defendants further urge the court to dismiss the plaintiff's RICO counts pursuant to Rule 12(6), for failure to

state a cause of action under the provisions of RICO; defendants argue there is no pattern of racketeering activity involved in the transactions at issue. The United States Supreme Court has recently interpreted RICO's pattern requirements. A party bringing an action under RICO must establish *both* a relationship between the predicate acts, and continuing racketeering activity.

> 'Continuity' is both a closed-and open ended concept, referring either to a closed period of repeated conduct, or to past conduct that by its nature projects into the future with a threat of repetition. It is, in either case, centrally a temporal concept - and particularly so in the RICO context, where *what* must be continuous, RICO's predicate acts or offenses, and the *relationship* these predicates must bear one to another, are distinct requirements. A party alleging a RICO violation may demonstrate continuity over a closed period by proving a series of related predicates extending over a substantial period of time. Predicate acts extending over a few weeks or months and threatening no future criminal conduct do not satisfy this requirement: Congress was concerned in RICO with long term criminal conduct. Often a RICO action will be brought before continuity can be established in this way. In such cases, liability depends on whether the *threat* of continuity is demonstrated.
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> *H.J. Inc. v. Northwestern Bell Telephone Co.*, 1989 U.S. LEXIS 3239, 7 (1989). (Citations omitted), (Emphasis in original).

See also *Management Computer Services, Inc. v. Hawkins, Ash, Baptie & Co.*, 1989 U.S. App. LEXIS 12908, 6 (7th Cir. 1989). Thus, the plaintiff must show that there is a relationship between the predicates acts, and that the predicates acts constitute continued racketeering activity, or that the predicates pose the threat of continuing racketeering activity. Applying

this to the facts presented in the plaintiff's complaint, although the plaintiff may be able to establish the necessary predicate acts, and the relationship to each other, (the defendants conspired and employed schemes to recover the minority shares outstanding at a price below a fair price), the plaintiff is unable to establish that such acts constituted *continuing* racketeering activity, or the threat of continuing activity.

Under a closed-end concept of continuity, the plaintiff is unable to establish a series of related predicates extending over a *substantial* period of time. The allegations of the complaint are that the predicate acts occurred in the spring of 1977, on May 5, 1977 and in the fall of 1977. The court finds that this time period is not substantial in light of *H.J. Inc.* In order to establish the continuity of the racketeering activity over a less than substantial period of time, the plaintiff must demonstrate that a threat of continuity exists. *Id.* In the amended complaint, the plaintiff has failed to demonstrate that, in spite of the required predicate acts, that such activity poses a threat of continuing fraudulent redemption of minority stock.

In that plaintiff is unable to establish a relationship between the predicates acts *and the threat of continuing racketeering activity,* Counts II, III and IV must be dismissed for failure to state a claim upon which relief may be granted.

COMMON LAW CLAIMS

The plaintiff has alleged several common law claims, in addition to her federal claims. In that this court's jurisdiction is based upon claims under federal statutes, which claims have, by this order, been dismissed before trial, the pendant state claims should be dismissed as well. *United Mine Workers v. Gibbs,* 383 U.S. 715, 726, 86 S.Ct. 1130, 1139, 16 L.Ed.2d 218 (1966); *Bieneman v. City of Chicago,* 864 F.2d 463, 470 (7th Cir. 1988).

CONCLUSION

Based upon the foregoing, the defendants' motion to dismiss as to all Counts must be, and the same hereby is granted.

IT IS SO ORDERED.

DATED: This 25th day of September, 1989.

/s/ William L. Beatty
United States District Judge